U.S. DEPARTMENT OF LABOR Employment and Training Administration Washington, D.C. 20213	CLASSIFICATION UI
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DIRECTIVE : UNEMPLOYMENT INSURANCE PROGRAM LETTER NO. 30-83

TO : ALL STATE EMPLOYMENT SECURITY AGENCIES

FROM : ROYAL S. DELLINGER
Administrator
for Regional Management

SUBJECT : Federal Unemployment Tax Credits for 1985 and Thereafter Under Recent Amendments to Federal Law

1. Purpose. To explain what amendments are needed to State laws as a result of the increase in the Federal taxable wage base to $7,000 with respect to wages paid for employment in 1983 and thereafter and the increase in the gross Federal tax and in the ceiling on total allowable credits against the Federal unemployment tax with respect to wages paid for employment in 1985 and thereafter.

2. References. P.L. 97-248 and UIPL 4-83.

3. Background. The taxable wage base with respect to wages paid for employment in 1983 and thereafter has been increased to $7,000. The gross Federal tax on such wages has been increased by 0.1 percent to 3.5 percent for 1983 and 1984. With respect to such wages paid in 1985 and thereafter, the gross Federal tax has been increased to 6.2 percent, and the total allowable credits have been increased to 5.4 percent against the gross tax. All of those changes in the Federal law will have significant consequences for employers in all States, especially those with experience rating.

4. State Laws. To assure that employers qualify for full allowable credits against the gross Federal unemployment tax with respect to wages paid for employment in 1985 and thereafter, SESAs should seek amendments to their laws, as appropriate, in the following respects.

a. The taxable wage base with respect to wages paid in 1983 and thereafter should be at least $7,000.

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DISTRIBUTION

b. The standard rate for experience rating purposes should be at least 5.4 percent with respect to wages paid in 1985 and thereafter.

c. All rates at 5.4 percent and below with respect to wages paid in 1985 and thereafter must be based on an employer's experience with his workers' risk of unemployment consistent with the requirements of section 3303(a)(1), FUTA, except as permitted under a transition provision mentioned below.

d. The transition provision, over a period of four years from 1985 to and including 1988, applies to a "specific industry provision" of a State law, as defined, and as explained in the attachment to this letter.

The reasons for, and an explanation of, the advice given above are contained in the attachment to this letter.

5. Action Required. SESAs should take timely action to assure amendment of their State laws as needed.

6. Inquiries. Inquiries may be directed to the appropriate regional office or to Ted Wagman on 202-376-7308 or Jim Segraves on 202-376-7052.

7. Attachment. Federal Unemployment Tax Credits and Experience Rating

Federal Unemployment Tax Credits and Experience Rating

The nature of the partnership between the Federal Government and the States in the unemployment compensation program is found most characteristically in their interrelated systems of taxation. An amount equal to the revenue derived from the Federal tax is appropriated to the Unemployment Trust Fund for use primarily to finance grants to the States for administration of their unemployment insurance laws and their employment service programs. The revenue derived from State taxes (contributions) is used for the payment of benefits to qualified unemployed individuals.

Employers subject to the tax imposed by section 3301 of the Federal Unemployment Tax Act (FUTA) with respect to having individuals in their employ may offset against that tax, currently in 1983 equal to 3.5 percent of taxable wages in the amount of $7,000, a credit pursuant to section 3302(a) of up to 2.7 percent of the contributions paid into the unemployment fund of a State certified by the Secretary of Labor under section 3304(c), FUTA. Employers may be granted "additional credit" pursuant to section 3302(b) under other conditions to be described below. Those conditions become particularly important for the States and employers subject to their laws when the offset credit ceiling is increased to 5.4 percent with respect to wages paid for employment subject to FUTA in 1985 and thereafter, as provided in section 271 of P.L. 97-248.

Section 3302(b), in effect, permits employers of a State with an approved law to credit against the Federal unemployment tax an amount of contributions paid by them into a State unemployment fund at a rate less than the rate at which credit is allowable pursuant to section 3302(a), commonly known as "normal credit," as though such reduced rate were equal to the rate at which normal credit is allowable. In other words, an employer with a "reduced rate" of contributions under a State's experience rating plan that satisfies the requirements of the Federal law with respect to granting reduced rates may credit against the gross Federal unemployment tax the full amount of the offset credit allowable if, in 1985 and thereafter, certain experience rating requirements are satisfied and the standard rate or the highest rate under experience rating, whichever is lower, is at least 5.4 percent.

There is an explicit linkage between section 3302(b) with respect to additional credit and section 3303(a) with respect to experience rating. Section 3302(b) provides that an employer may take additional credit against the Federal unemployment tax, if the State law satisfies the experience rating requirements of section 3303(a) and "if throughout such 12-month period, he had been subject

under such State law to the highest rate applied thereunder in the 12-month period to any person having individuals in his employ /i.e. any subject employer,/ or a rate of 2.7 percent /or 5.4 percent for 1985 and thereafter,/ whichever rate is lower." (Emphasis added). Section 3303(a) provides that an employer "shall be allowed an additional credit under section 3302(b) with respect to any reduced rate of contributions permitted by a State law, only if the Secretary of Labor finds that under such law" (emphasis added) reduced rates of contributions to a pooled fund are permitted only under an approved experience rating plan.

The term "reduced rate" is defined in section 3303(c)(8) as "a rate of contributions lower than the standard rate applicable under the State law, and the term 'standard rate' means the rate on the basis of which variations therefrom are computed." (Emphasis added). The "standard rate" is thus crucial to a determination of what rates are reduced rates within the context of experience rating requirements. Since additional credit with respect to contributions paid in 1985 and thereafter will be permitted to employers of a State at a maximum rate of 5.4 percent of taxable wages or the highest rate applied under the State's approved experience rating plan, whichever rate is lower, and since additional credit is allowable only with respect to a reduced rate, it is important that a State's standard rate for such period be no less than 5.4 percent. Since the "standard rate" is the rate on the basis of which variations therefrom are computed, it must be a rate that is assignable to an employer on the basis of his experience under the State's experience rating plan. This is significant in relation to the maximum additional credit that is allowable because under section 3302(b), the amount of additional credit in 1985 and thereafter will be the highest rate applied under experience rating (i.e., a computed rate) or 5.4 percent, whichever rate is lower.

It is apparent from the foregoing description of the Federal law provisions governing the allowance of additional credit and experience rating that the emphasis is upon the rates of contributions assessed subject employers. The taxable wage base is relevant, in contrast, to the amount of allowable normal credit. If in 1983, for example, when the taxable wage base is increased to $7,000, a State's taxable wage base remains at $6,000, all employers who pay contributions at rates lower than 3.15 (which yields the same amount as a rate of 2.7 percent on a taxable wage base of $7,000) will lose a portion of the allowable normal credit. Even employers who qualify for additional credit in 1983 will be granted normal credit of only 2.7 percent on taxable wages of $6,000 in the example given.

If a State prefers not to permit reduced rates of contributions or suspends experience rating to preserve the solvency of its unemployment fund, the rate or rates at which its subject employers

pay contributions should be no less than 5.4 percent for 1985 and thereafter, or there will be a loss of normal credit.

If a State's taxable wage base is higher than the Federal taxable wage base of $7,000 in 1985, it will nevertheless be necessary for the State's standard rate under experience rating to be no less than 5.4 percent if all of the State's employers are to receive the full additional credit allowable under the Federal law. A yield of contributions under a State standard rate lower than 5.4 percent applied to a taxable wage base higher than $7,000 will not necessarily qualify all of the State's employers for the full amount of additional credit allowable under the Federal law since wages actually paid may be less than the higher taxable wage base. It will, therefore, produce a lower yield than the nominal State taxable wage base.

Section 3302(c)(1), FUTA, provides, as amended, that the total credits allowable under section 3302--normal and additional credits--for a taxable year on and after 1985 "shall not exceed 5.4 percent" of the total taxable wages subject to the Federal unemployment tax.

With respect to 1985 and thereafter, contribution rates of 5.4 percent and below must satisfy the experience rating requirements of section 3303(a)(1), FUTA. If a State's schedule of rates contains rates higher than 2.7 percent which are not assigned to employers on the basis of experience or which do not satisfy, in one or more respects, the requirements of the Federal law, the State agency should seek amendment to its law. Such rates above 2.7 percent should be rates computed by the same factors as used in computing the rates at and below 2.7 percent. There is one exception in the form of a limited transition provision.

Section 271(c)(3) of P.L. 97-248 provides that additional credit will be allowed for up to four years, from 1985 through and including 1988, despite rates of contributions granted at and below 5.4 percent which are not based on experience, if such rates are granted under a "specific industry provision," as defined. There are four conditions all of which must be satisfied for a rate to qualify under that exception. Such a rate must:

1. Have been granted pursuant to a provision in the State law in effect on August 10, 1982.

2. Apply to employees in a specific industry or to an otherwise definable category of employees.

3. Be a rate higher than 2.7 percent which is not based on experience and which employers may elect, i.e., which is not

mandatory, for the payment of contributions.

4. Be increased in the years 1985 through and including 1988 by at least 20 percent of the difference between such rate (in effect prior to 1985) and 5.4 percent so that with respect to 1989, or earlier, and thereafter all rates assigned to employers at 5.4 percent and below will be based on an employer's experience.